

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA
SACRAMENTO DIVISION

In re)	Case No. 10-35071-A-12
PRATT VINEYARDS, LLC,)	Docket Control No. SAC-5
)	Date: June 2, 2011
Debtor.)	Time: 10:00 a.m.
)	

MEMORANDUM

The debtor moves to confirm its amended chapter 12 plan. Secured creditor ReProp Investments opposes that plan's confirmation, arguing that it is not feasible in light of the debtor's past financial performance. It also argues that the interest rate proposed for its secured claim remains "below the rate for similar type loans and provides no upward adjustment for the numerous risks associated with financing the debtor's loan."

The court will confirm the amended plan and overrule the objections. Because the plan will be confirmed, it will deny ReProp's motion either to dismiss the case or grant it relief from the automatic stay.

I

The court continued the confirmation hearing to May 24, asking the debtor to brief several issues, including whether the debtor would have the ability to refinance ReProp's loan at the end of the five-year plan term, and ReProp's objections concerning expenses the debtor had allegedly omitted from its financial projections. The debtor addressed these issues in

1 several documents filed to support confirmation of the plan.

2 At the request of the parties, the confirmation hearing was
3 continued once again to June 2, 2011. In connection with the
4 second continuance, the court gave no party leave to file
5 anything further in support of, or in opposition to, confirmation
6 of the amended plan. Nonetheless, on May 26 the debtor filed two
7 additional declarations. The court will not consider these
8 declarations.

9 The court disagrees with the debtor that ReProp's
10 declarations filed on April 15 were similarly filed without leave
11 of court. At the hearing on April 11, the court specifically
12 authorized ReProp to a response to the evidence filed on April 6
13 by the debtor. See Docket 172.

14
15 II

16 Turning to the merits, the court concludes that the amended
17 plan is feasible as required by 11 U.S.C. § 1225(a)(6).

18 First, with respect to the alleged understatement of taxes,
19 as pointed out by the debtor, its revenue is generated mainly by
20 nontaxable sales or services, including nontaxable grape sales,
21 nontaxable wine client services, nontaxable out-of-state retail
22 Internet wine sales, and nontaxable wholesale sales to bars and
23 restaurants. The only taxable sales identified by the debtor are
24 retail wine sales. Docket 195 at 5. This explanation satisfies
25 the court. The debtor's financial projections do not materially
26 understate this expense.

27 Second, with respect to the debtor's ability to refinance
28 the property securing ReProp's claim, the debtor argues that

1 ReProp is undersecured. The debtor asserts that the property
2 securing ReProp's claim has a value between \$700,000 and
3 \$720,000. ReProp claims it is owed \$719,250. Hence, the
4 debtor's argument that ReProp is under-secured may or may not be
5 the case.

6 Using the declaration of David Bolster, the debtor contends
7 that the property securing ReProp's claim will appreciate "2%-5%"
8 in value in the next five years, to "the low to upper
9 \$800,000's." However, appreciation in value from \$700,000 to the
10 low to upper \$800,000's is not an appreciation of 2% to 5%. This
11 appreciation exceeds 15% (an increase from \$700,000 to \$810,000
12 is 15.7%).

13 More important, while the declaration of David Bolster
14 includes his October 2010 valuation of the property, that
15 valuation is inconsistent with the debtor's claim that ReProp is
16 undersecured. According to David Bolster's Broker's Price
17 Opinion (BPO), the value of the property is \$823,000, making
18 ReProp an over-secured creditor, even without considering whether
19 ReProp is secured by the debtor's personal property. See May 6,
20 2011 Bolster Decl.

21 The debtor also argues that ReProp should be estopped from
22 claiming that it is oversecured because ReProp has repeatedly
23 claimed that it is undersecured.

24 However, the debtor is the one who has the burden to
25 establish plan feasibility, ability to refinance at the end of
26 the proposed plan term, and the value of the property. This is
27 not ReProp's burden of proof and thus, even if ReProp is estopped
28 to claim that it is oversecured, that does not somehow establish

1 that ReProp is undersecured. In other words, regardless of what
2 ReProp claims, the court must determine the value of the property
3 based on the evidence presented by the debtor.

4 In this case, the evidence presented by the debtor, namely,
5 the declaration of David Bolster incorporating the BPO from
6 October 2010, supports the conclusion that ReProp is oversecured.
7 According to its proof of claim, ReProp was owed \$719,250 as of
8 the petition date. David Bolster's BPO says that the property
9 has a value of \$823,000. And, although the BPO is dated October
10 2010, the court concludes that the value of the property was
11 higher than \$719,250 as of the June 8, 2010 petition date, just
12 four months prior to the BPO date. The property did not
13 appreciate in excess of \$100,000 in the period of approximately
14 four months, between the petition date and the BPO date.

15 Therefore, the court disagrees with the debtor that ReProp
16 is undersecured. The court concludes that ReProp is oversecured
17 and entitled to post-petition, pre-confirmation interest at the
18 contract rate, 12.5%, for the eleven months that have passed
19 since the petition date.

20 The interest on \$719,250 is approximately \$82,414. Thus,
21 ReProp's claim as of May 2011 is \$788,575 ($(\$719,250 + \$82,414) -$
22 $\text{three adequate protection payments totaling } \$13,089$). Upon plan
23 confirmation, the debtor will make a \$90,000 payment, further
24 reducing ReProp's claim to \$698,575 ($\$788,575 - \$90,000$). Then,
25 the debtor will make 59 payments of \$5,180 to ReProp, further
26 reducing the principal to approximately \$592,418.64.

27 If the property does not appreciate beyond its current
28 \$823,000 value, the debtor would have approximately 28% equity in

1 the property ($100 - (\$592,418 / \$823,000 \times 100)$). And, if the
2 property appreciates to \$900,000, as argued by the debtor, there
3 would be approximately 34.2% equity in the property ($100 -$
4 $(\$592,418 / \$900,000 \times 100)$). The court has no evidence refuting
5 David Bolster's opinion that the property is likely to appreciate
6 2% to 5% by the end of the five-year plan term.

7 An equity cushion of 28% to 34% will significantly increase
8 the likelihood of a refinance of the property at the end of the
9 five-year plan term. The court is satisfied that the debtor has
10 a reasonable chance of obtaining a refinance and satisfying
11 ReProp's claim in full.

12 Third, with respect to the expenses ReProp maintains were
13 omitted from the debtor's financial projections, the court is
14 satisfied that the debtor has explained their absence.

15 For the most part, the debtor has absorbed those expenses by
16 having its principals, Mr. and Mrs. Pratt, perform work that is
17 often outsourced by other wineries. See, e.g., May 6, 2011 David
18 Pratt Decl. Also, the debtor's vineyard operation is relatively
19 small, ten acres, allowing Mr. and Mrs. Pratt to do much of the
20 work themselves. For instance, the maintenance and repair of
21 equipment are minimal because Mr. Pratt does the work himself.

22 Id. The same is true with the year-round care for the vineyard.

23 Id. Except for the grape-picking, the Pratts do most of the
24 work. This explains the low contract labor expense projected by
25 the debtor.

26 It also explains the decrease in cost of goods sold and
27 inventory. The debtor is producing its own wine inventory and
28 its principals are doing most of the labor themselves.

1 The court further notes that the debtor's monthly \$652
2 equipment lease with Bank of the West expires in September 2012.
3 This means that in 15 months the debtor's monthly expenses will
4 decrease by \$652.

5 As to fees for licenses and permits, the debtor has based
6 its projections on a single \$1,250 fee in 2010. This translates
7 into approximately \$104 per month. Such fees are included in the
8 \$166 per month allocated for accounting expenses. See May 6,
9 2011 David Pratt Decl.

10 As to the debtor's projected accounting expenses, they are
11 less than the debtor's accounting expenses in 2010 for two
12 reasons. In 2010, the expenses included accounting expenses
13 associated with the filing of the debtor's bankruptcy case. This
14 case was filed on June 8, 2010. Post-confirmation, however, the
15 debtor will not have such expenses. Also, during some of 2010,
16 the debtor's vineyard and winery businesses were two separate
17 entities, each with its own separate accounting records and tax
18 returns. See Docket 153, Ex. F. These two entities have been
19 consolidated thereby eliminating the duplicative accounting
20 expense.

21 The court concludes that the projected monthly accounting
22 expense of \$62 (\$166 total accounting expenses minus \$104 for
23 licenses and permits) is sufficient to cover the debtor's likely
24 post-confirmation accounting expense.

25 As to promotion expenses, the debtor has stated that this
26 item includes "wine used for pouring at events, pouring in the
27 tasting room, and donations for fundraising." These expenses are
28 included in the projected \$165 per month for miscellaneous

1 supplies. See May 6, 2011 David Pratt Decl. While the debtor
2 spent more on promotion in 2010 than the projected \$1,980 in
3 annual promotion expenses (\$165 x 12 months) under the plan, the
4 court is not convinced that the debtor has underestimated or
5 omitted these expenses. As noted earlier, the debtor is
6 producing its own inventory of wine and is able to provide of its
7 own wine at promotional events at a lower cost.

8 Fourth, the court rejects the argument that Mrs. Pratt's
9 full time employment precludes her from devoting time in the
10 operation of the winery and its tasting room. The Pratt's
11 Schedules I and J from their chapter 13 bankruptcy case (Case No.
12 09-36899), indicates that Mrs. Pratt is an independent contractor
13 earning \$1,500 per month. Case No. 09-36899, Docket 1. The fact
14 that she is an independent contractor and receives only \$1,500 a
15 month suggests that her employment other than in the debtor's
16 winery and tasting room is part time.

17 Finally, the debtor has been in this bankruptcy proceeding
18 for approximately 12 months and has shown that it is able to
19 generate sufficient cash to make the payments called for under
20 the proposed chapter 12 plan. The debtor has accumulated cash
21 during the pre-confirmation period at a rate sufficient to fund
22 the plan. See Docket 170, Ex. B.

23 The court is satisfied with the feasibility of the debtor's
24 proposed plan.

25 III

26 The proposed 6.25% interest rate to be paid on ReProp's
27 secured claim is sufficient to pay it the present value of its
28 claim as required by 11 U.S.C. § 1225(a)(5)(B). Because ReProp's

1 claim will be paid over a 5-year period, this means that the plan
2 must provide that its claim will accrue interest at an
3 appropriate rate.

4 Under Till v. SCS Credit Corp., 541 U.S. 465 (2004) the
5 appropriate interest rate is determined by the "formula
6 approach." This approach requires the court to take the national
7 prime rate in order to reflect the financial market's estimate of
8 the amount a commercial bank should charge a creditworthy
9 commercial borrower to compensate it for the loan's opportunity
10 costs, inflation, and a slight risk of default.

11 The bankruptcy court is required to adjust this rate for a
12 greater risk of default posed by a bankruptcy debtor. This
13 upward adjustment depends on a variety of factors, including the
14 nature of the security, and the plan's feasibility and duration.
15 Cf. Farm Credit Bank v. Fowler (In re Fowler), 903 F.2d 694, 697
16 (9th Cir. 1990); In re Camino Real Landscape Main. Contrs., Inc.,
17 818 F.2d 1503 (9th Cir. 1987).

18 To set the appropriate rate, the court is required to
19 conduct an 'objective inquiry' into the appropriate rate. The
20 debtor's bankruptcy statements and schedules may be culled for
21 the evidence to support the appropriate interest rate.

22 "Moreover, starting from a concededly *low* estimate and
23 adjusting *upward* places the evidentiary burden squarely on the
24 creditors, who are likely to have readier access to any
25 information absent from the debtor's filing. . . ." Till at 479.

26 The prime rate on the petition date, June 8, 2010, and on
27 the date of the confirmation hearing, was 3.25%. See
28 www.moneycafe.com/library/primerate.htm. As surveyed by the

1 Supreme Court in Till, courts using the formula approach
2 typically have tended to adjust the prime rate 1% to 3% to
3 account for credit risk peculiar to the specifics of a case.


4 The proposed rate of 6.25% is sufficient. The court so
5 concludes for a variety of reasons. First, the proposed rate is
6 well above the prime rate. Second, the court is convinced that
7 the debtor will be able to perform its plan. Third, the
8 objecting creditor's collateral is primarily real estate. There
9 is no evidence before the court that its collateral has
10 depreciated or is likely to depreciate during the five-year term
11 of the plan. Fourth, at the end of five years, the debtor will
12 likely be able to refinance the property and will pay ReProp's
13 loan in full. Finally, the amended plan includes a significant
14 lump sum payment, \$90,000, further reducing the risk to ReProp
15 and adequately protecting its interest in its collateral.

16
17 IV

18 For the foregoing reasons, the amended plan will be
19 confirmed, the objections to confirmation will be overruled, and
20 ReProp's motion to dismiss the case or for relief from the
21 automatic stay will be denied. Counsel for the debtor shall
22 lodge conforming orders.

23 Dated: *June 2011*

24 By the Court

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26 _____
27 Michael S. McManus, Judge
28 United States Bankruptcy Court